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NOTES.

CONTRACTS—RESTRAINT OF TRADE—VALIDITY OF A SYSTEM OF CONTRACTS SEEKING TO CONTROL THE PRICE AT WHICH AN ARTICLE SHALL BE RESOLD.—Contracts seeking to control the price at which an article shall be resold are of two types. In contracts of the first type, the manufacturer undertakes to maintain a uniform price by putting into effect what may be characterized as the “rebate plan” whereby the manufacturer promises to refund to dealers maintaining the selling prices fixed by the producer, a portion of the purchase price paid by them. This, while operating as an inducement to the dealer to resell only at the price named, in no way binds him to do so. And this type of contracts has been uniformly upheld.¹ Of the second type are the various kinds of contracts employed in what may be described as the “contract system.” The simplest form of this type is where the maker affixes to every package of his article a notice that the goods may be resold only at certain prices. In another simple form it consists of contracts between

¹ *In re Greene*, 52 Fed. 104 (1894); *Clark v. Frank*, 17 Mo. App. 602 (1885); *Walsh v. Dwight*, 58 N. Y. Supp. 91 (1899).

the manufacturer and wholesaler, whereby the latter agrees to supply the trade at a stated price, and to sell only to dealers who will maintain the fixed retail price. In another variant form, which, however, has been held only colorable,² the contract with the wholesaler purports to make him a distributing agent for the producer. In the final phase of the evolution of this system the contract with the wholesaler requires him to sell only to dealers approved by the manufacturer, with whom the manufacturer contracts directly, that, in consideration of their being supplied with his product, they will not sell below the fixed retail price. This was the system adopted by the producer of a so-called "patent" medicine, in *Dr. Miles Medical Co. v. Park & Sons Co.*; ³ and the Supreme Court held the contract void as being an illegal restraint of trade, both at common law and under the Sherman Act.

The true test by which the legality of a contract requiring the purchaser to resell at a fixed price is to be determined is (1) whether the stipulation is of an ancillary nature; (2) whether it affords only a reasonable protection to the business of the covenantee; and (3) whether such a stipulation, considered with reference to the benefit to the public arising from the production of the article, as well as the detriment to the public in being deprived of the benefit of free competition, as to the selling price, is, upon the whole, against public interest.⁴ It is not the fact of restraint, but the degree of the restriction which will control; and in the last analysis the question as to the validity of a particular contract will be found largely one of expediency.⁵ This common law principle is not peculiar to "trade-secret" articles, but is equally applicable to any chattel property. But it must be remembered that the court was not dealing with a single contract, in the principal case, but with a system of contracts covering the entire production of the complainant, and the reason which might uphold covenants restraining the liberty of a single buyer might prove quite inadequate where there are a multitude of similar agreements. The single covenant might in no way affect the public interest, when many such agreements might.⁶

It is well settled that articles covered by patents may be the subject of contracts by which their price in subsale is controlled by the patentee; and that such contracts, if otherwise valid, are not within the rules of the common law against monopolies and re-

² See *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 164 Fed. 803 (C. C. A., 1908).

³ 220 U. S. 373 (1911).

⁴ *Edgar Lumber Co. v. Cormie*, 130 S. W. 452 (Ark., 1910); *Hubbard v. Miller*, 27 Mich. 15 (1873); *Roberts v. Lamont*, 102 N. W. 770 (Neb., 1905); *Merriman v. Cover*, 51 S. E. 817 (Va., 1905).

⁵ *Nordenfelt v. Maxim Nordenfelt & Co.*, 1904 A. C. 565; *Gibbs v. Consolidated Gas Co.*, 130 U. S. 396 (1889).

⁶ *Park v. Hartman*, 153 Fed. 24 (C. C. A., 1907).

straint of trade.⁷ Until very recently the doctrine prevailed that the manufacturer of "trade-secret" articles had similar rights.⁸ This mistaken conception resulted from an apparent similarity between the conditions surrounding articles manufactured under "trade-secrets" and those manufactured under patents; and from a failure to distinguish between the sale of a secret formula and the sale of the articles manufactured therefrom. Since the decision in the principal case it can no longer be doubted that the exemption extended to patented articles does not apply to "trade-secret" products.⁹

The trading-stamp¹⁰ and railroad ticket¹¹ cases have frequently been cited in support of a system of contracts like that in the principal case. But these cases rest upon the peculiar character of the property rights involved. Neither concerns the buying and selling of articles of general commerce; and both relate to things in the nature of contracts personal in character, and not to things which can ever become the subject of general trade and traffic. Like all contracts personal in their nature, they can be transferred and assigned only

⁷ *Bement v. National Harrow Co.*, 186 U. S. 70 (1902). It has been suggested that the relation of the patent cases to the general subject may be more clearly understood by saying that the circumstance that the promisee has been granted a legal monopoly does not, in fact, create an exemption from the general operation of the rule, but rather brings them within the exception existing in the case of ancillary stipulation reasonably necessary to the protection of a party to a legitimate business transaction.

⁸ *Fowle v. Park*, 131 U. S. 88 (1889); *Dr. Miles Med. Co. v. Platt*, 142 Fed. 606 (1906); *Miles v. Jayne*, 149 Fed. 838 (1906); *Garst v. Harris*, 177 Mass. 72 (1900); *Park v. National Wholesale Druggists' Assn.*, 175 N. Y. 1 (1903).

⁹ In *Hartman v. Park*, 145 Fed. 358 (1906), Judge Cochran, although he sustained a system of contracts similar to the one in the principal case, concluded that secret process articles were no more exempt from the common law rule against restraints of trade than any other article of manufacture. This case was reversed on appeal, *Park v. Hartman*, 153 Fed. 24 (C. C. A., 1907), but in his opinion in this case and in *Dr. Miles Co. v. Park*, 164 Fed. 803 (C. C. A., 1908), Mr. Justice Lurton (then Circuit Judge) states the law in these strong terms: "Any other conclusion would be to sanction a monopoly in that class of goods vastly more far reaching than the monopoly extended upon high grounds of public policy to the inventor. The statutory monopoly has a limitation of a few years. To obtain it the inventor must put on record his invention. At the end of the term the public will be free to employ the discovery without the burden theretofore imposed as a compensation to the inventor. Not so with the monopoly asked for by those who control the enormous proprietary trade of this country. Their monopoly will go on forever, and, if there be merit in the formula, they may not only preserve it thru all time, but continue to restrain prices and prevent competition in the sale of the product." See also *Grogan v. Chaffee*, 156 Cal. 611 (1909), and *W. H. Hill & Co. v. Gray & Worcester*, 163 Mich. 12 (1910).

¹⁰ *Sperry & Hutchinson Co. v. Mechanics' Clothing Co.*, 135 Fed. 833 (1904).

¹¹ *Nashville Ry. Co. v. McConnell*, 82 Fed. 65 (1897).

with the assent of both contracting parties and only upon the conditions to which the contracting parties assent.¹²

Many of the decisions *contra* to the principal case have treated cases holding that authors have a common law right in their compositions before publication, and cases recognizing a similar property in news or information, as authorities for the proposition that a manufacturer may control the resale price of his product. It is submitted that the principles underlying the cases are not analogous. It is the policy of the law to reward individual thought and research by protecting the enjoyment of their fruits: thus the author,¹³ the news gatherer,¹⁴ and the owner of an unpatented invention¹⁵ are protected against the piratical use of their peculiar property. A similar protection is extended to the chemist who has discovered a secret formula.¹⁶ But it does not follow that because a secret process or formula will be protected against betrayal by those to whom it has been communicated in confidence under a contract for a restricted use, that a system of contracts for the control of all sales and subsales of the article when produced will be outside of the rules in restraint of trade, simply because it is the product of such secret formula.

So the cases analogous to the invention, composition and news cases are those in which a secret process or formula is protected; not cases in which the owner of the secret is attempting to control all resales of the finished article. The principal case recognizes this distinction. Though irreconcilable with some of the earlier cases,¹⁷ it is in accord with the more recent decisions;¹⁸ and certainly appears to be sound.

C. L. M.

¹² *Bitterman v. Railroad Co.*, 207 U. S. 205 (1907); *Park v. Hartman*, *supra*; *Hill v. Gray & Worcester*, *supra*.

¹³ *Donaldson v. Beckett*, 4 Burrows K. B. Rep. (1774); *Palmer v. Dewet*, 47 N. Y. 532 (1872).

¹⁴ *Exchange Tel. Co. v. Gregory* (1896) 1 Q. B. 147; *Board of Trade v. Christie*, 198 U. S. 236 (1905); *Dodge v. Information Co.*, 183 Mass. 62 (1903).

¹⁵ *Peabody v. Norfolk*, 98 Mass. 452 (1868); *Tabor v. Hoffman*, 23 N. E. 12 (N. Y., 1889).

¹⁶ *Harrison v. Glucose Co.*, 116 Fed. 304 (C. C. A., 1902); *Thum v. Tloczynski*, 114 Mich. 149 (1897); *Salomon v. Hertz*, 40 N. J. Eq. 400 (1885); *Tode v. Gross*, 127 N. Y. 480 (1891); see also *Maxim Nordenfelt v. Nordenfelt* (1893) 1 Ch. D. 630, for a review of the English cases.

¹⁷ *Ellimon Co. v. Carrington* (1901) 2 Ch. D. 275; *Grogan v. Chaffee*, *supra*; *Garst v. Charles*, 187 Mass. 144 (1905); *Ice Co. v. Park*, 21 How. Pr. 302 (N. Y., 1861). See also cases cited under note (8), *supra*.

For the real basis for the decision in *Park v. Nat. Wholesale Druggists' Assn.*, *supra*, see *Straus v. American Publishers' Assn.*, 177 N. Y. 473 (1904), opinion by Parker, C. J., who wrote a concurring opinion in the *Park* case.

¹⁸ *Park v. Hartman*, *supra*; *Dr. Miles Co. v. Park*, *supra*; *Hill v. Gray & Worcester*, *supra*.